February 2, 2005

CERTIFIED MAIL
RETURN RECEIPT REQUESTED

Reference Number.: 05-0008

Mrs. Sue Hess
President
Brewer Fence, Inc.
1345 Ellisville Boulevard
Laurel, MS 39940

Dear Mrs. Hess:

This is in response to the appeal that you filed on behalf of your firm, Brewer Fence, Inc. ("Brewer Fence"). We have carefully reviewed the material from the Mississippi Department of Transportation ("MissDOT") as well as information you provided and concluded that the denial of your firm's certification as an eligible Disadvantaged Business Enterprise (DBE) under criteria set forth in 49 CFR Part 26 ("the Regulation") is supported by substantial record evidence.

Your appeal is denied based upon our determination that substantial evidence supports MissDOT's conclusion that your contribution of capital to acquire ownership interest in the firm was not real, substantial, and continuing within the meaning of the Regulation.

The specific reasons for the denial of your appeal include the following:

BACKGROUND

The record indicates MissDOT first denied the firm DBE certification in January 2004. Following the firm's appeal, the Department remanded the matter back to MissDOT on July 15, 2004, instructing MissDOT to determine the structure and relationship, as well as your ownership, of Brewer Fence (the applicant firm) and related divisions ---------- . The Department also asked MissDOT to assess your control of the firm and address specifically your job duties, experience, and activities at Brewer Fence and its two divisions. According to the record MissDOT conducted a second on-site review of the firm on August 11, 2004, and held a second DBE Committee hearing to address these issues. (The exact date of this hearing is not noted in the record, and is referenced in this decision as "summer 2004

hearing.") On September 23, 2004, MissDOT again denied the firm DBE certification, basing this decision solely on ownership grounds. Since MissDOT did not address the control issues as requested by the Department in its July 2004 remand, this decision will only address whether substantial evidence supports MissDOT's conclusion that your ownership in the firm was not real, substantial, and continuing as required by the Department's Regulation.

In both its original January 2004 and Summer 2004 DBE Committee hearings, MissDOT explored the history of how Brewer Fence and its divisions were capitalized by both you and your husband, ----------, a non-disadvantaged individual and the firm's Secretary; as well as the circumstances of how you acquired your percentage of stock. Both hearing transcripts along with the record form the basis for the Department's decision.

OWNERSHIP

According to the Regulation at §26.61(b), the firm seeking certification has the burden of demonstrating to you, by a preponderance of the evidence, that it meets the requirements of this subpart concerning group membership or individual disadvantage, business size, ownership, and control.

The Regulation at §26.69(b) states that to be an eligible DBE, a firm must be at least 51 percent owned by socially and economically disadvantaged individuals.

The Regulation at §26.69(c) provides in part, that contributions of capital or expertise by the disadvantaged owner to acquire an ownership interest in the participating DBE business be real and substantial and continuing, going beyond pro forma ownership of the firm as reflected in ownership documents.

The Regulation at §26.69(h)(1) states that you must presume as not being held by a disadvantaged individual, for purposes of determining ownership, all interests in a business or other assets obtained by the individual as the result of a gift, or transfer without adequate consideration, from any non-disadvantaged individual or non-DBE firm who is (i) involved in the same firm for which the individual is seeking certification, or an affiliate of that firm; (ii) involved in the same or a similar line of business; or (iii) engaged in an ongoing business relationship with the firm, or an affiliate of the firm, for which the individual is seeking certification.

The Regulation §26.69(i) states, in part that you must apply the following rules in situations in which marital assets form a basis for ownership of a firm. When marital assets (other than the assets of the business in question), held jointly or as community property by both spouses, are used to acquire the ownership interest asserted by one spouse, you must deem the ownership interest in the firm to have been acquired by that spouse with his or her own individual resources, provided that the other spouse irrevocably renounces and transfers all rights in the ownership interest in the manner sanctioned by the laws of the state in which either spouse or the firm is domiciled.

1. According to the Summer 2004 hearing record, you indicated that you purchased Brewer Fenceworks in August 1993 with a $15,000.00 loan from ---------- and a personal note for $40,000.00. You stated that the $15,000.00 was used for operation expenses and $40,000.00 for equipment and assets. The record contains a copy of the purchase agreement for this transaction. It specifies that the purchase price for the assets was $1,192.05. and that you and Mr. Hess, as the firm's new owners, would pay the firm's sole creditor, ----------. You stated:

> Sue Hess: ---------- was financing Brewer Fenceworks, it's the company that we bought and Mr. Brewer had run into some difficulties paying his bills actually so ---------- was more than interested in selling the company to someone else and carrying the loan.
> [MissDOT Representative]: So he had initially financed Brewer Fence prior to your being involved with it.
> Sue Hess: Correct
> [MissDOT Representative]: So . . . it was almost like a continuation of the loan?
> Sue Hess: Right

During the latter part of the hearing, you indicated that a portion of the $55,000.00 investment was used to purchase trucks, a computer fence program for $3,500.00, and additional items

2. ---------- , operating in ------- , Mississippi, was purchased in 2000. You indicated during the hearing that this company was purchased with a loan from the previous owners, --- . and ---------- and -- ---------- ; and that collateral for the loan was secured by jointly owned rental property. During MissDOT's Summer 2004 hearing, the following exchange took place:

> Sue Hess: For Lindsey Fence, I arranged the note with -------- and ---------- -------- and they carried that note.
> [MissDOT Representative]: And that was for what amount?
> Sue: $276,000 and $93,000 whatever that total is, it's two separate.
> [MissDOT Representative]: Was there any collateral you allowed in these notes?
> Sue Hess: Not on, Fenceworks, it was signature only on ----------, yes, property that we jointly owned.
> [MissDOT Representative]: Joint property, was that your personal home?
> Sue Hess: Rental
> [MissDOT Representative]: Rental property

The record contains two "multipurpose note and security agreements" dated July 1, 2000. This first agreement obligates Brewer Fence to pay ---------- $240,000.00. Under the second agreement the firm agreed to pay ---------- $97,500.00.

3. According to the firm's application, you own 53 percent of company stock. You indicated in MissDOT's January 20, 2004 hearing that you set up the company with you owning 80 percent ownership interest and ---------- having 20 percent ownership interest, however; this figure was changed to 53/47 because of retirement reasons. You stated in your February 3, 2004, rebuttal letter:

> My only explanation for the $10 fee we each paid to purchase the stock is I took the advice of the attorney hired to draw up the corporate paperwork. While it is true that my husband and I contributed the same amount of $10 for the purpose of common, privately held stock, when the corporation was formed, it was I as President of the newly formed corporation that devised a business plan, projected budget, met with attorneys and lending institutions and had the proper documents executed. I arranged for the initial loans with ---------- . . . to purchase Brewer Fence company, and all subsequent loans. . . The denial letter from [MissDOT] states that I claim to own 53 percent of the stock. Our corporate and personal tax returns were submitted and demonstrate that I am indeed enjoying the customary incidents of ownership and sharing in the risks and profits commensurate with my ownership interests.

During MissDOT's summer 2004 hearing, you clarified that you sold your husband the additional 27 shares for $1.00 per share.

4. Under the Regulation §26.69(c), the disadvantaged owner must enjoy the customary incidents of ownership, and share in the risks and profits commensurate with their ownership interest. A firm's president generally receives greater compensation than the firm's employees. The record is unclear as to whether you receive the highest compensation in the firm. Although you indicated during the hearing that both you and ---------- , a non-disadvantaged individual, each earn ---------- per year, you indicated that both of you may be receiving stock dividends. You stated:

> In that K-1, I think that's what it's called, that we get each year. I'm sure that's what it's called that shows the percentage of stock and what that is. But the stock dividend if we choose to take the stock dividend . . . they tax on whether we take it or not. But if we choose, to then we decide on how much we want to take also and add it to the same percentage. Say if we were going to take --------- , I get -------- and some change and he gets about that much.

5. You alleged at the hearing that you personally incurred a loan for Brewer Fence's Bobcat. Although it was through the company, you indicated that the purchase was made using your personal credit card. You also indicated that this credit card is only used for business expenses and is shared by your husband, Cliff Hess.

6. There is little information contained in the record concerning Brewer Fence's acquisition of Fenceworks. Although it was described during MissDOT's January 20, 2004 hearing, the record remains unclear.

7. In your October 13, 2004 rebuttal letter, you stated:

> The denial letter states: "*The source of start-up capital used for the purchase of the two companies that make up Brewer Fence, Inc.,* ---------- *and* ---------- *, came from a joint source of income. These companies and/or*

> *their equipment were purchased with loans secured jointly by both owners*." This is a true statement. Although I am the President and at start-up held 80% of the shares, the lending institutions insisted that ---- - sign the agreement prior to any funds being disbursed. If a corporate loan defaults, I am responsible for 80% of the remaining balance, therefore, even thought the loan was secured by both owners, the percentage of debt load was not an equal amount. . . . .
>
> The denial letter states: "*The purchase of the owner's stock shares appears to have come from the joint account of both owners, as well.*" I was not questioned about this. How does it appear to have come from a joint account? If I had been questioned, I would have responded that in July of 1993, when the corporation was set up, the original stock purchase was from separate accounts. We had separate accounts as I was an independent contractor. . . . I ceremoniously purchased the 80 share of stock and deposited the money into the company's original cash drawer. ----- then purchased his 20 shares of stock and deposited the money in the cash drawer. Our tax records from 1993 will indicate this fact. I did not provide or elaborate on this issue as our tax records indicate that me, the majority owner, has always received form 1120 (schedule K-1) from the corporation indicate I have received my proper percentage of shareholder's share of income, credits, deductions, etc. It is true that we currently have a joint account, but, again, tax records show that I have contributed the larger percentage of funds into that account through the K-1's.
>
> The denial letter quotes [the Regulation] §26.69(i)(1). The ownership interest was not secured by community property. The ownership interest, as stated above, was deposited from individual accounts into the cash drawer. This paragraph doesn't apply to my ownership interest at all. . . .

The Regulation §26.69(c) requires a disadvantaged business owner in a firm to contribute real and substantial capital or expertise to obtain their ownership in the business. Based on the record evidence, it does not appear that you made a real and substantial contribution to acquire your ownership interest in Brewer Fence, ---------- , or ---------- . It appears that joint funds were used belonging to both you and your husband Cliff Hess, a non-disadvantaged individual, in combination with various loans secured by both of you. As you indicated in your rebuttal letter, your initial cash contribution was ceremoniously purchased by depositing money into the company's cash drawer. The record is void of any substantive evidence to support this transaction and contains no evidence that your contribution of capital to acquire your ownership interest was derived from your personal funds. We must therefore, conclude that your investment does not meet the requirements of the Department's Regulation. In addition, to acquire your ownership interest, you alleged that the purchase of the firm's property, such as the Bobcat, was made using your own personal credit card. This is also not real and substantial contribution of capital within the meaning of the Regulation. Lastly, to support your claim of ownership, you alleged above that you receive income, credits and deductions based on your percentage of ownership in the firm, as evidenced by K-1 statements. This also fails to meet the requirements of the Regulation since the intention of the program is to look to a disadvantage owner's contribution at the inception of a firm and not owners' proceeds.

Substantial record evidence therefore supports MissDOT's determination that his contribution of capital was not real and substantial and did not meet the requirements of the Department's Regulation.

OTHER ISSUES

In its remand letter, the Department noted that the firm was certified as small disadvantaged business by the Small Business Administration ("SBA") on September 26, 2002. The Department stated:

> During the DBE Committee meeting, there is a passing reference that SBA's documentation regarding the firm has been lost and that MissDOT proceeded to re-gather the information. There is no indication that this certification was appropriately considered by MissDOT in its certification denial. In addition, we are unclear as to which of the three firms the SBA certification was applicable.

The record contains a copy of SBA's certification for Brewer Fence, Inc. Under the Department's Regulation §26.84, recipients must conduct an on-site review of firms that are SBA certified and certify the firm as a DBE unless, based on the on-site review and other information, the firm does not meet the eligibility requirements of the Department's DBE program. The Department agrees with MissDOT's determination that the firm is not eligible for the program based on the record evidence.

In summary, the information provided cumulatively supports a conclusion that Brewer Fence does not meet the criteria as required for DBE certification under 49 CFR Part 26. The company is, therefore, ineligible to participate as a DBE on MissDOT's Federal financially assisted projects. This determination is administratively final as of the date of this correspondence.

Sincerely,

Joseph E. Austin, Chief
External Policy and Program Development Division
Departmental Office of Civil Rights

cc: MissDOT